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Agenda Item 6c

March 15, 2011

TO: MEMBERS OF THE BENEFITS AND PROGRAM ADMINISTRATION COMMITTEE

I. SUBJECT: SB 439 (Negrete McLeod) – As Introduced
Limits on Gifts and Travel

Sponsor: State Controller

II. PROGRAM: Legislation

III. ANALYSIS:

Summary

As introduced, SB 439 prohibits all CalPERS and CalSTRS Board Members and employees required to file Statements of Economic Interests (also known as Form 700), including consultants, from accepting gifts valued in excess of $50 from any single source in a single calendar year. In addition, the bill would establish sanctions for vendors or contractors who made gifts in violation of this policy twice in a five-year period.

At the time of this writing, the sponsor's office has expressed its intent to amend SB 439 to clarify that the provisions of this bill apply only to: 1) individuals who are required to file Form 700's; and 2) gifts from entities that have had business with CalPERS or CalSTRS within the past five years, or who intend to seek to do business with the Retirement Systems.

Background

Existing State Law

Specified State and local government officials and employees must file a Form 700 annually, disclosing information about the sources of a public official's income, investments, business positions, real property holdings and gifts. Reporting an economic interest is not a conflict in itself; a conflict arises when the official makes a governmental decision that impacts their economic interests. The Political Reform Act of 1974 (PRA), among other things, imposes limits on gifts, prohibits honoraria payments, and imposes other restrictions on the receipt of travel and personal loans by State and local officials and candidates for office that are required to file a Form 700. Currently, gifts from certain sources may not exceed $420 in a calendar year, and personal loans from sources listed in a required filer's Form 700 may not exceed $250 per calendar year. Under the PRA, gifts from a single source that aggregate $50 or more must be disclosed on the official's Form 700. The PRA has established exceptions from the definition of gift, e.g., gifts from certain family members, informational material, among many other exceptions. Failure to report gifts, honoraria, loans, and travel payments pursuant to the PRA may result in monetary penalties of up to $5,000 per violation.

When an agency's conflict-of-interest code requires its Form 700 filers to disclose income and gifts only from specified sources, gifts from sources that are not required to be disclosed are not subject to the $420 gift limit. Most high-ranking CalPERS employees and investment personnel, however, have an unlimited reporting category as "public officials who manage public investments."

Pursuant to the Public Employees Retirement Law (PERL), the CalPERS Board of Administration (Board) may not consider matters involving vendors or contractors in a closed session without full written disclosure by the vendor or contractor of their: campaign contributions aggregating two hundred fifty dollars ($250) or more, and any gifts aggregating fifty dollars ($50) or more during the preceding calendar year to any member of the Board. Failure to disclose provides a basis for disqualification of the contractor or the vendor.

Last year, CalPERS co-sponsored Chapter 668 (AB 1743, Hernandez), to require placement agents to register as lobbyists, making them subject to strict reporting and ethics rules specified in the PRA, and enforced by the Fair Political Practices Commission (FPPC). Placement agents must now file quarterly activity reports detailing any honoraria, gifts, fees or other compensation, and attend biennial ethics classes. Among other things, the PRA prohibits lobbyists from making campaign contributions, and limits their gifts to CalPERS Board Members and officials to $10 per calendar month.

<u>CalPERS Policies</u>

The CalPERS No Gift Policy for staff (Policy), adopted in November 2009, prohibits employees that are required to file a Form 700 under its Conflict of Interest Code (including, among others, system executives, divisions chiefs and investment professionals) from accepting anything of value including, without limitation, money, gifts, services, loans, entertainment, tickets, transportation, food or beverages from any person or entity doing business with CalPERS; seeking to do business with CalPERS; or who is the type of entity that does business with CalPERS. At the onset, there were numerous questions on implementation of this new Policy that have been resolved through FAQ's and training. Questions and answers are continuously provided on the Insider.

At its October 20, 2010 meeting, the Board adopted a new Form 700 and Travel Transparency Policy that requires all Form 700s and certain Board and staff travel information to be posted on the CalPERS internet web site.

In addition to the Gift Policy, the CalPERS Statement of Incompatible Activities prohibits all CalPERS board members and employees from receiving or accepting any gifts from “anyone who is doing or is seeking to do business of any kind with the Public Employees’ Retirement System or whose activities are regulated or controlled by PERS under circumstances from which it reasonably could be substantiated that the gift was intended to influence the officer or employee in his or her official duties or was intended as a reward for any official actions performed by the officer or employee.”

CalPERS has also opened a secure Ethics Helpline, which provides a way for individuals to safely and confidentially report concerns about conduct that may be unethical, illegal, or in violation of professional standards.

Proposed Changes

Specifically, SB 439 would:

- Reduce the annual statutory limit on gifts from any single source[1] from $420 to $50 for CalPERS and CalSTRS Board Members and employees and consultants required to file a Form 700.

- Disqualify any vendor or contractor violating the $50 limit twice in a five-year period from bidding on or receiving any contract for a two-year period, from the date of the conviction of the Board or employee for receipt of the second gift.

Legislative History

2010 Chapter 668 (AB 1743, Hernandez – Requires placement agents to register as lobbyists and be subject to the strict reporting and ethics rules applicable to lobbyists under the PRA. Requires placement agents, placement agent firms and placement agent employers to register and report quarterly on their activities including any honoraria, gifts, fees or other compensation. *CalPERS Position: Co-sponsor.*

[1] The sponsor intends to amend this to any entity that has had business with CalPERS or CalSTRS within the past five years, or who intend to seed to do business with CalPERS or CalSTRS.

2009 Chapter 301 (AB 1584, Hernandez) – Among other things, requires the disclosure of campaign contributions and gifts made by placement agents to public retirement board members. *CalPERS Position: Support.*

1998 Chapter 923 (SB 1753, Schiff) – Requires campaign disclosure for CalPERS Board candidates and incumbents. It also requires vendors or contractors to provide written disclosure of campaign contributions aggregating $250 or more and gifts aggregating $50 or more to any member of the Board, officer, or employee of the system before the Board considered in closed session any matter in which they are involved. *CalPERS Position: Support.*

Issues

Arguments in Support

According to the author, "California's public pension systems are the largest in the country and should be held to a higher standard…Limiting gifts from individuals and organizations trying to influence the decisions of pension boards and government employees is the right thing to do."

According to the sponsor, "The appearance of impropriety by some former Board Members and investment staff of CalPERS raises concerns that Board Members and staff may be using their past relationships and positions of power to influence decisions regarding the investment of public pension funds…I believe these bills *(SB 439 and AB 873)* are a critical step toward restoring the public's confidence in the professionalism of all of our activities on behalf of the retired public employees and teachers, and the taxpayers of California."

Organizations in support: State Controller John Chiang (Sponsor), Common Cause, AFSCME, SEIU.

Arguments in Opposition

There is no known opposition at this time.

Special Review Recommendations

At the December 2010 Board meeting, staff presented the findings and recommendations of an independent special review, led by Steptoe & Johnson LLP, to investigate and address issues raised by the use of placement agents by external investment managers, and determine whether their payment of placement agent fees and related activities compromised the interests of CalPERS participants and beneficiaries.

While the independent review recognized CalPERS stringent new policies on gifts and travel, it also recommended "that this step be reinforced by enhanced training and certifications and that similar policies be adopted to apply to its Board members. Failure to comply with CalPERS gift and travel policies should have disciplinary consequences not only for staff or Board members, but also for the external manager or other firm in question. Going forward, either contractually or by regulation or legislation, any firm involved in two or more violations of these gift and travel policies should be prohibited from doing business with CalPERS for a period of not less than two years."

Impact on CalPERS Employees and Consultants

In its current form SB 439 would prohibit any CalPERS employee or consultant required to file a Form 700 from accepting a gift over $50 from any single source regardless of connection to CalPERS. As stated earlier, the sponsor is intending to amend the bill to instead prohibit gifts from entities that have had business with or intends to have business with CalPERS. This amendment would be narrowly tailored to address the issues raised by the Special Review.

Impact on Business Partners

Any person who makes a gift in violation of the PRA is liable in a civil action brought by the FPPC for amount of up to three times the amount of the unlawful gift. In addition, SB 439 would expressly disqualify any vendor or contractor that violates the gift limits twice in any five year period, from bidding on, or being awarded any contract for a period of two years following the date of the conviction of the recipient of the second gift.

Staff recommends a more flexible remedy for vendors and contractors found to be in violation of the gift policy. An alternative option would be to add this history to the criteria used to determine future actions and dealings with that vendor, such as contract amendments or extensions. This would provide flexibility for the Board to deal with past, present and future business partners who may have made immaterial or inadvertent violations to the policy and yet balance with its fiduciary interests.

Policy vs. Statute

CalPERS already has a no gift policy in place for employees required to file a Form 700. The Board could always adopt a more stringent gift policy than current law provides for Board members and consultants required to file a Form 700. The advantages of a gift limit in statute are that it provides greater certainty and independent enforcement authority by the FPPC, for example.

Summary of Gift Policies of Other Large Public Pension Funds

The proposed new limit is similar to, or consistent with the goals of gift policies for retirement systems in ten other states. A chart summarizing these policies is below.

System	Summary
CalSTRS	No gifts greater than $390 in the aggregate per year.
Connecticut State Treasury	No gifts greater than $10 each and $50 in the aggregate. No food or beverage greater than $50 per year.
Illinois TRS	No gifts that might affect or appear to affect judgment.
Iowa PERS	No gifts from "restricted donor."
LA CERA	No gifts from anyone doing or seeking business from LACERA.
North Dakota PERS	No gifts greater than $50 from anyone doing or soliciting business on behalf of NDPERS.
New York City	No gifts over $50 from anyone soliciting or doing business with the City.
New York STRS	No gifts other than nominal gifts.
Ohio PERS	No gifts.
Ohio STRS	No gifts from persons doing business with OSTRS and no travel expenses.
Pennsylvania SERS	No gifts other than *de minimis* gifts.
SWIB	No gifts, subject to limited exceptions.
TRS of Texas	No gifts greater than $50, subject to exceptions.
Washington SIB	No gifts greater than $50, subject to exceptions.

Legislative Policy Standards

The Board of Administration's Legislative Policy Standards do not directly address the issues posed by SB 439.

IV. STRATEGIC PLAN:

This is not a product of the CalPERS strategic plan, but an ongoing responsibility of the CalPERS Office of Governmental Affairs.

V. RESULTS/COSTS:

Program Costs

None.

Administrative Costs

Possible added workload for the Office of Enterprise Compliance to monitor and investigate reports of violations of the $50 gift limit.

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